

California's Budget Crisis



Daniel J.B. Mitchell

May 7, 2009

UCLA-SPA

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Los Angeles Times

U.S. EDITION

100¢ (U.S. ONLY)

They're drinking it up in N.Y.

The city's upstart beer scene is booming, and a new craft brewery is set to open in the city's heart.

In a city where the only thing that's been going up is the price of everything, a new craft brewery is set to open in the city's heart. The city's upstart beer scene is booming, and a new craft brewery is set to open in the city's heart.

The city's upstart beer scene is booming, and a new craft brewery is set to open in the city's heart. The city's upstart beer scene is booming, and a new craft brewery is set to open in the city's heart.

'We will rebuild, we will recover'

Obama tells Congress that changes to healthcare, energy policy are key



President Barack Obama, Vice President Joe Biden and Speaker of the House Nancy Pelosi at a news conference after Obama's first address to Congress.

OFFERING HOPE FOR ECONOMY

Obama's first address to Congress was a message of hope and optimism.

Obama's first address to Congress was a message of hope and optimism. He told Congress that he would work to create jobs and rebuild the economy.



Obama's first address to Congress was a message of hope and optimism. He told Congress that he would work to create jobs and rebuild the economy.

A little sun peeks through the clouds

The president's message of hope and optimism was a welcome sight.

The president's message of hope and optimism was a welcome sight. He told Congress that he would work to create jobs and rebuild the economy.

The president's message of hope and optimism was a welcome sight. He told Congress that he would work to create jobs and rebuild the economy.

The president's message of hope and optimism was a welcome sight. He told Congress that he would work to create jobs and rebuild the economy.

For Britney, it's her father's prerogative

Britney Spears' father is in charge of her career and finances.

Britney Spears' father is in charge of her career and finances. He has been her manager since she was a teenager.

Britney Spears' father is in charge of her career and finances. He has been her manager since she was a teenager.



A golfer swinging a club on a golf course.

Could a big swing?

The golfer's swing is the key to his success.

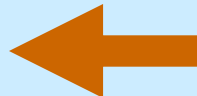
The golfer's swing is the key to his success. He has been a professional golfer for many years.

SOUTHERN CALIFORNIA FORECLOSED HOME AUCTION

Saturday, March 7 • Pomona Fairplex

VIEW ALL HOMES AT ZETABID.COM | 1-800-4-2ETABID

OPEN HOUSES THIS WEEKEND



California's Budget Crisis

CALEEFORNEEYA

by Rex Babin



Daniel J.B. Mitchell
May 7, 2009

California's Budget Crisis

CALEEFORNEEYA

by Rex Babin



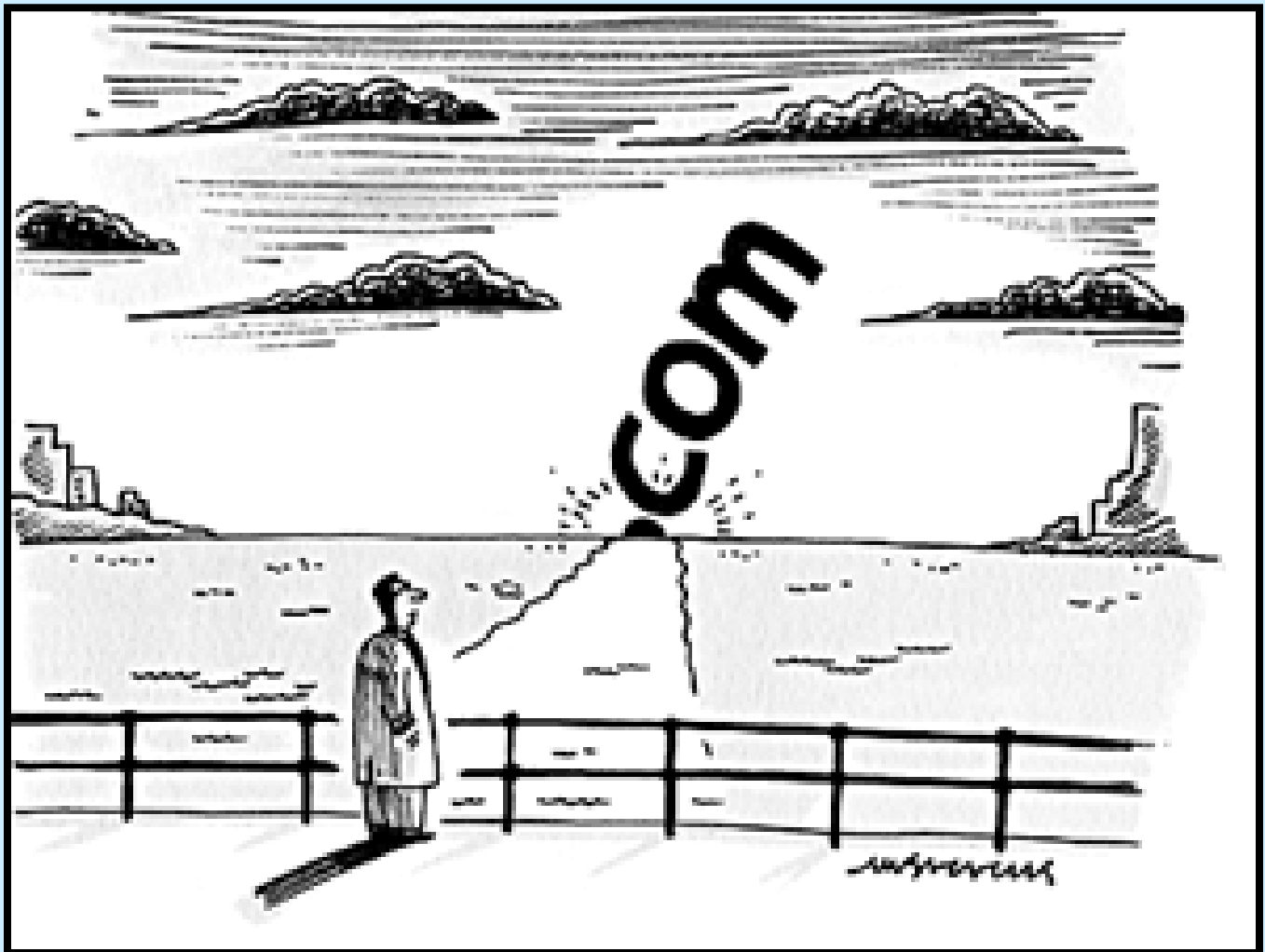
Daniel J.B. Mitchell
May 7, 2009

California's Budget Crisis



May 7, 2009

Or did we know?

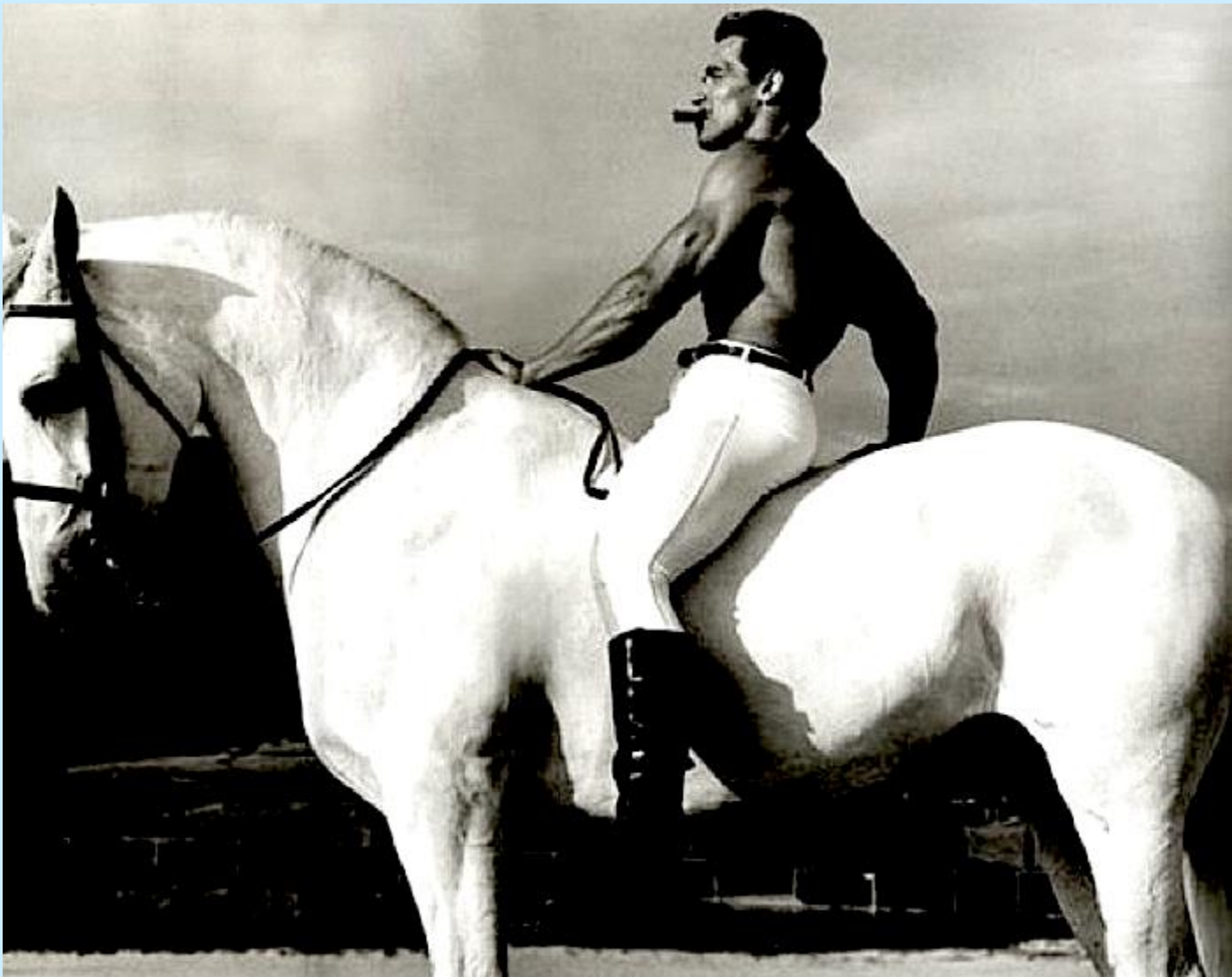


Or did we know?



supposed to be
Repetition is a teacher





The Man on the White Horse Syndrome?



The Man on the White Horse Syndrome?

FORTUNE

DISPLAY UNTIL APRIL 6, 2009

CAN MEG WHITMAN SAVE CALIFORNIA?

THE FORMER CEO OF EBAY GEARS UP TO RUN FOR GOVERNOR
BY PATRICIA SELLERS
PAGE 64

INSIDE THE WORLD'S BIGGEST HEDGE FUND

BY BRIAN O'KEEFE
PAGE 71

MEL KARMAZIN FIGHTS TO RESCUE SIRIUS

BY JON BIRGER
PAGE 84

Meg Whitman
and Brandy,
Half Moon Bay, Calif.
March 7, 2009

FORTUNE.COM

Woman on a Non-White Horse?



*Is the current budget crisis
an unpleasant surprise?*



Two scenarios



**Did the budget problem
just creep up when no
one was looking?**



Bird Scenario



**Or did we really know
what was happening?**



***Casablanca
Scenario***



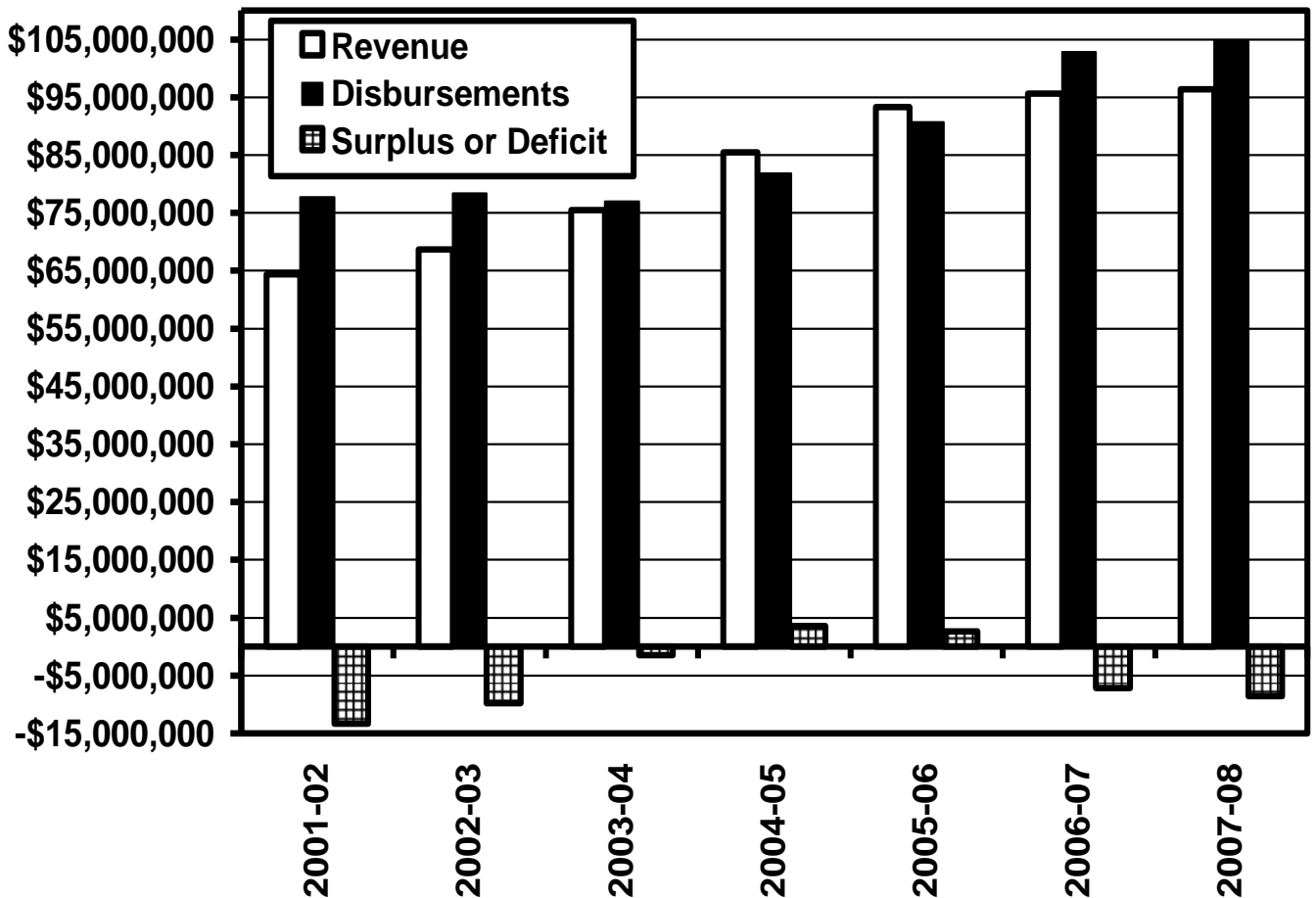
Or did we really know what was happening?



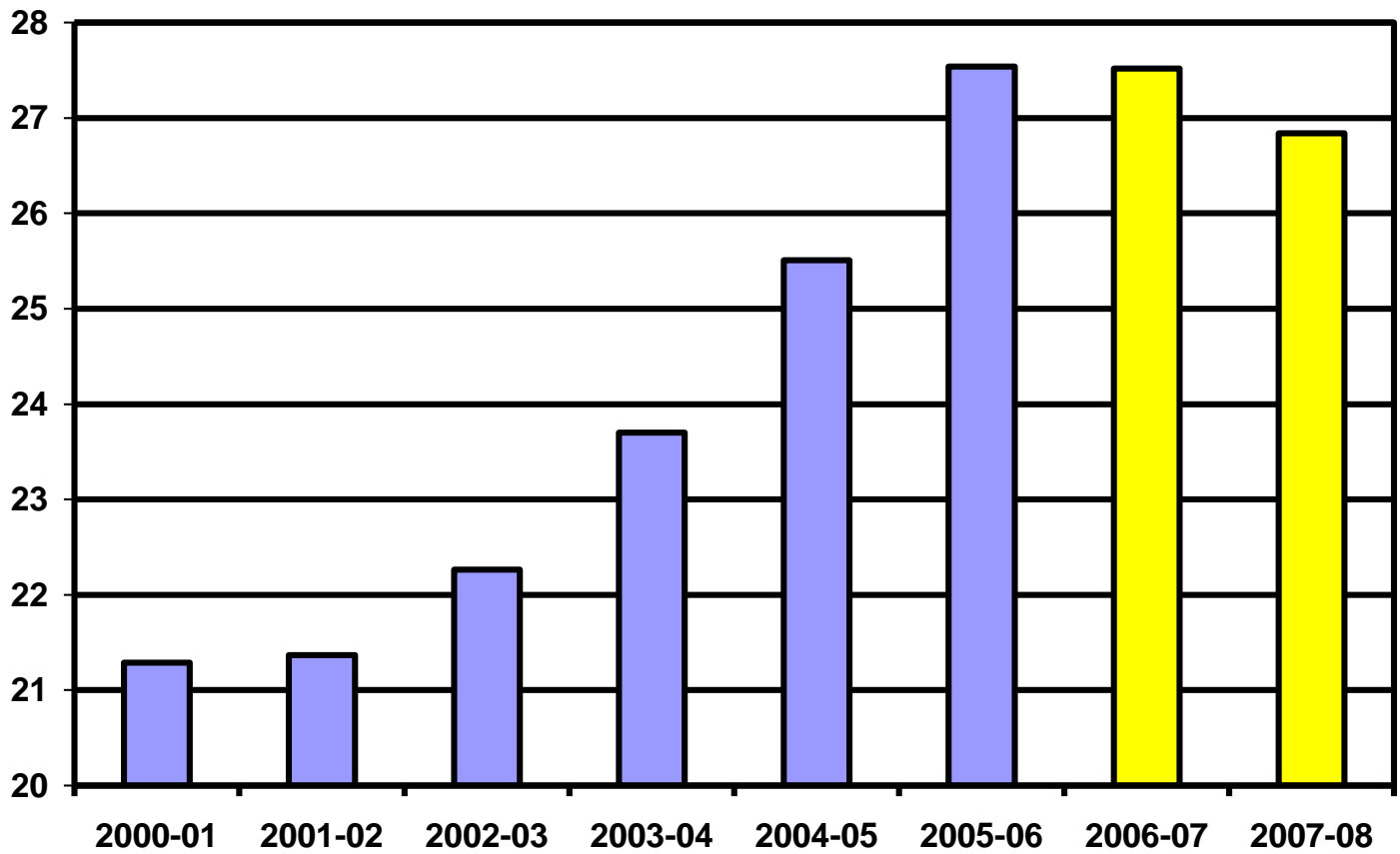
Looking Backwards Before the 2008-09 Crisis



Adjusted Cash Statement (\$000)



California Sales Tax: \$Billions



Brant Ward / The Chronicle



March 26, 2007



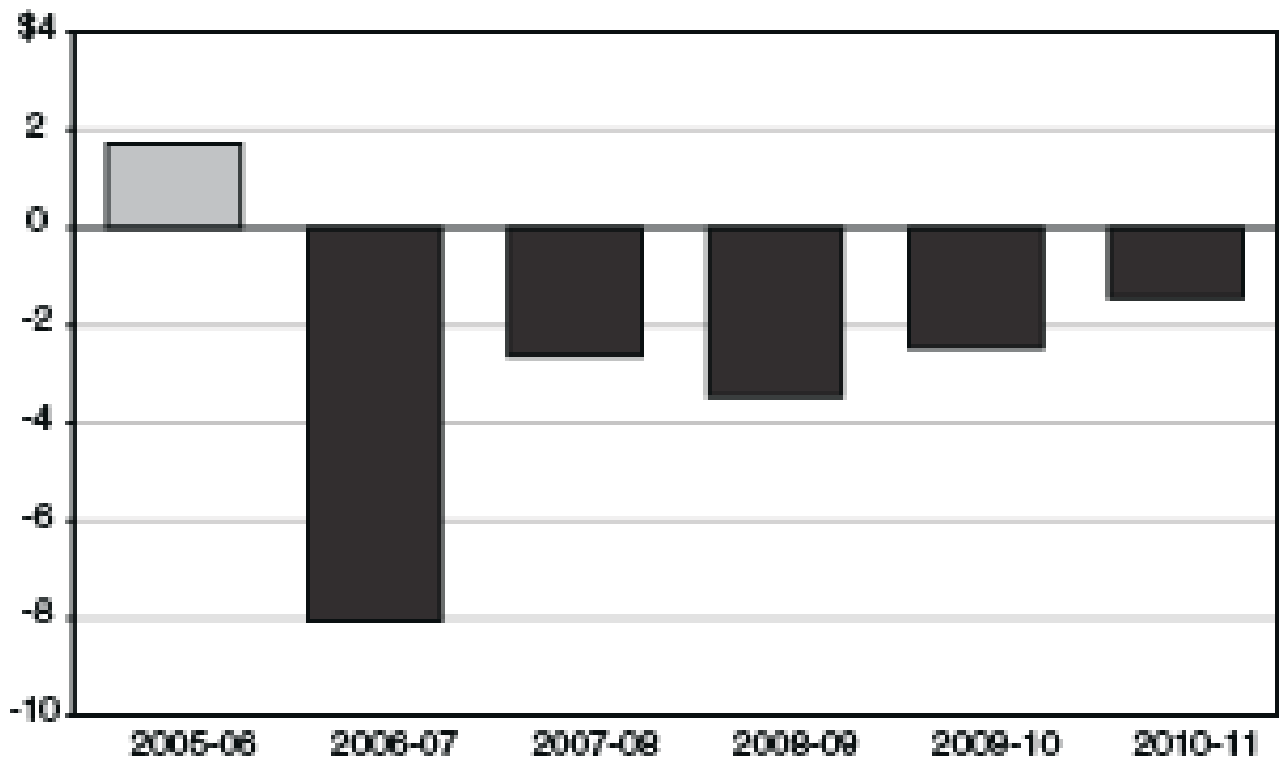
LAO Projections as of mid-Feb. 2007



Deficits

Significant Operating Shortfalls^a Would Remain

General Fund (In Billions)



^aAnnual revenues minus expenditures. Legislative Analyst's Office estimate of Governor's revenue and expenditure policies.

**When you are at the
peak, you can't fall up**



L.A. UNLEASHED

ALL THINGS ANIMAL IN SOUTHERN CALIFORNIA AND BEYOND

Stone-throwing Santino the chimp shows apes can carry out plans

7:35 PM, March 9, 2009



A chimpanzee named Santino has shown researchers that the great apes can plan ahead and execute carefully plotted maneuvers. Santino, the alpha male chimp at Sweden's Furuvik Zoo, planned rock-throwing attacks against zoo visitors, which shocked zoo staff and fascinated scientists.

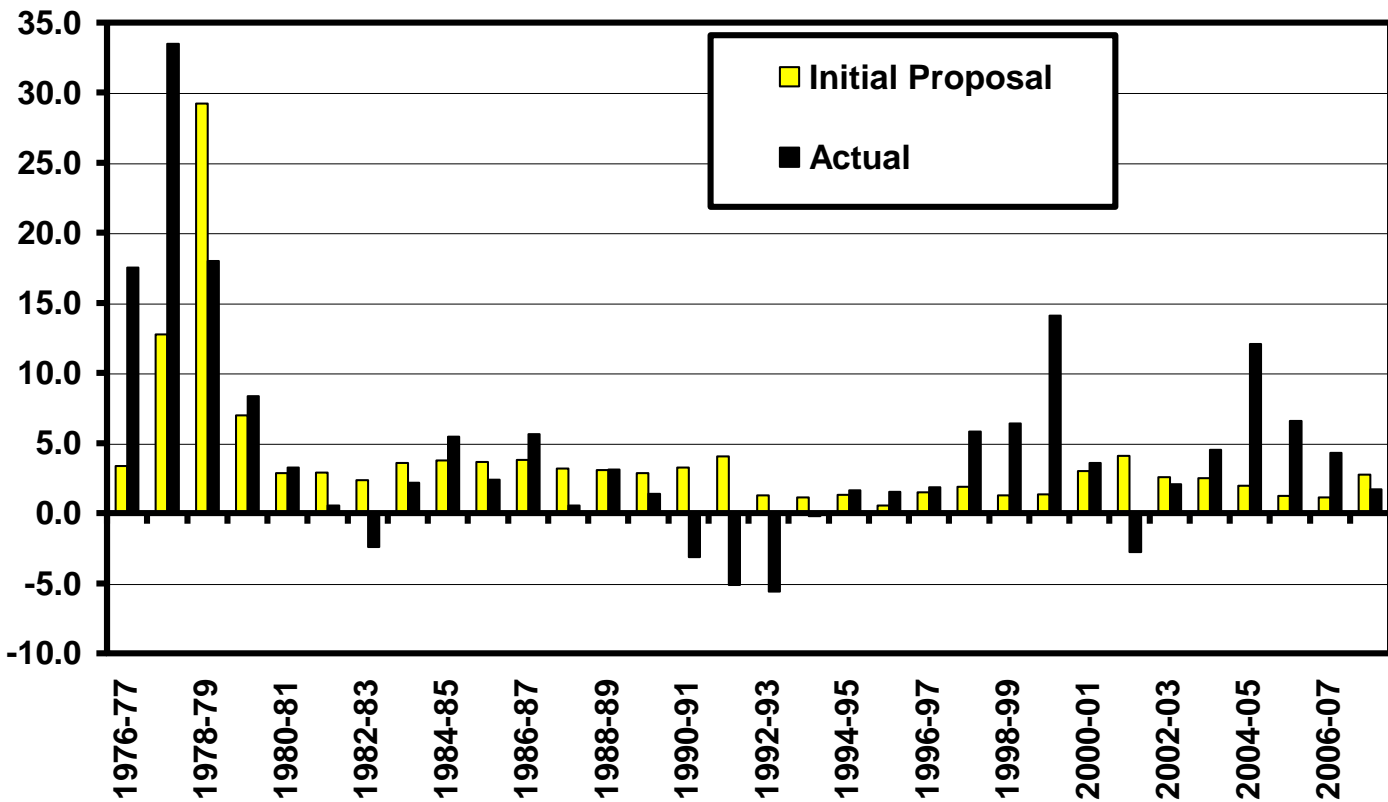


THE CALIFORNIA VOTER



Overoptimistic forecasts?

Initial Proposal and Actual Result:
FY General Fund Reserves as % of Expenditures



Over 32 years:

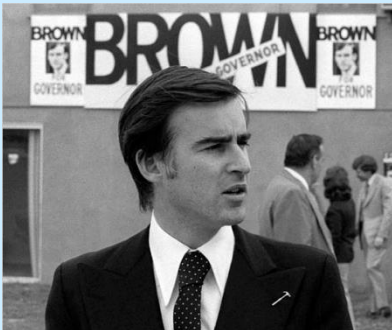
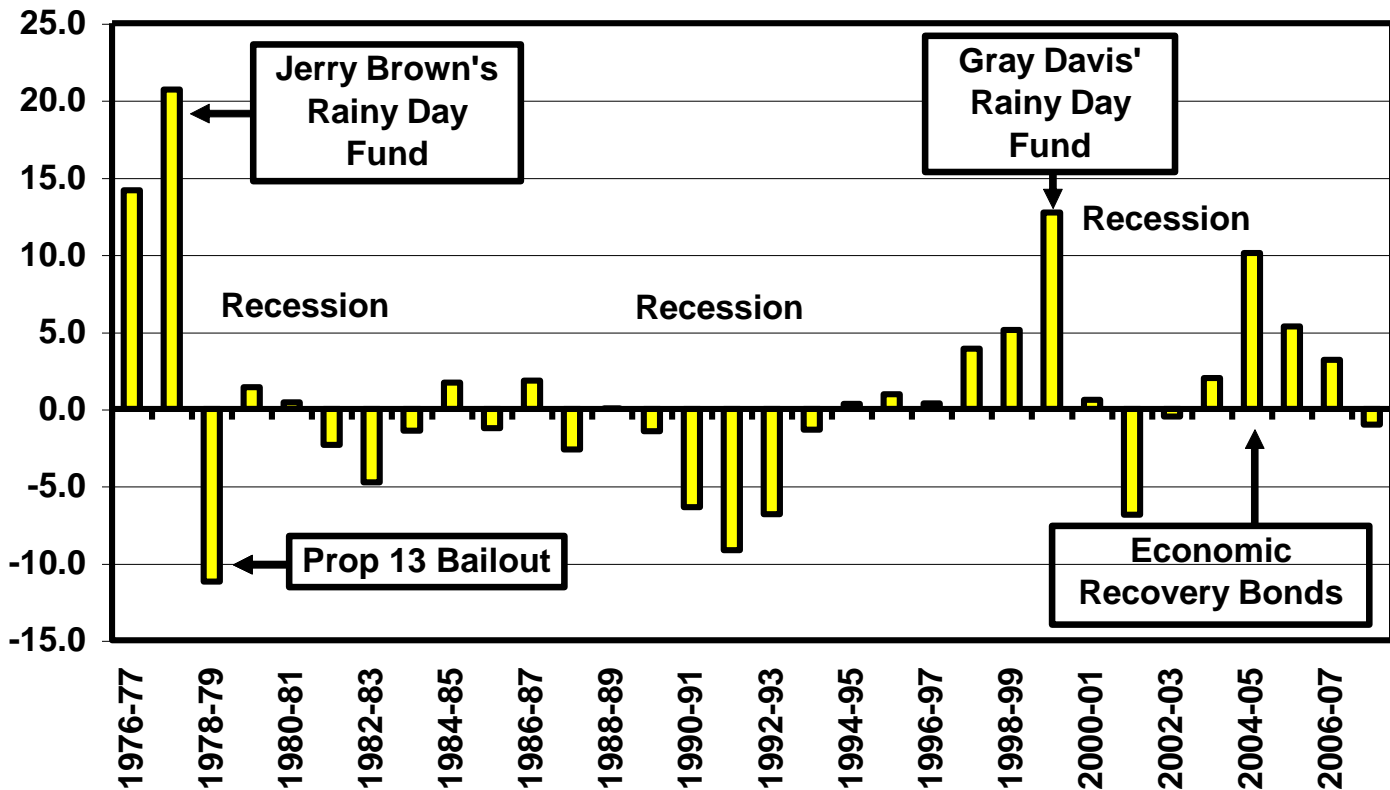
Average: 0.9% underestimate

Median: 0.3% underestimate

Note: Some underestimates
due to later borrowing to
raise reserve.



Actual - Initially Proposed GF Reserve as % of Expenditures



In recessions, we tend to overestimate.



State Budget 101





State Budget 101

Transparency

- On the web?
- Promote understanding?





State Budget 101

Transparency

- On the web? (Grade A)
 - Promote understanding?
- Depends on definitions**

California Home Department of Finance Governor's Web Site Department Index Site Map Help Thursday, October 23, 2008

Welcome to California's

GOVERNOR'S BUDGET 2008-09

Enacted Budget Summary

Home

Enacted Budget Summary

Summary Charts
Revenue Estimates
Major Program Areas

Enacted Budget Detail

K thru 12 Education
Higher Education
Health and Human Services
Corrections and Rehabilitation
Business, Transportation & Housing Resources
Environmental Protection
State and Consumer Services
Labor and Workforce Development
General Government
Legislative, Judicial, and Executive

Budget References

eBudget Search



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ebudgetwebmaster@dof.ca.gov

Enacted Budget Summary

The Enacted Budget Summary reflects the state spending plan passed by the Legislature and signed by the Governor. The Enacted Budget Summary provides [Summary Charts](#), [Revenue Estimates](#), Enacted Budget Summary information for selected [Major Program Areas](#), and veto messages.

[Budget Overview](#)
[Printable Budget Documents](#)

 To access the entire Enacted Budget Summary document (including veto messages) in a printable format (pdf), click here:
[Enacted Budget Summary - All Chapters](#) (pdf * - 1052K)

BUDGET OVERVIEW [Back to Top](#)
[Introduction](#)

The 2008 Budget Act resolves the \$24.3 billion budget deficit identified in the May Revision. It provides a modest reserve of \$1.7 billion this year, but projects a deficit of \$1.0 billion in 2009-10. While this budget does not resolve the state's persistent structural budget deficit, it includes a historic budget reform measure that puts California on the path to fiscal stability and avoids borrowing from local governments or transportation funds.

 Go to the [Enacted Budget Detail](#) web pages.

PRINTABLE BUDGET DOCUMENTS [Back to Top](#)
[Enacted Budget Summary - All Chapters](#) (pdf * - 1052K) -
Provides the entire Enacted Budget Summary in pdf format. Veto messages are included at the end of this printable document.

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 **Adobe Reader** pdf* This file requires the latest Adobe Acrobat reader plugin. If you do not have it - [click here](#) to download.

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State Budget 101

Transparency

Promote understanding? Depends on definitions

- Cash Statement Definitions from Controller Especially with Regard to “Borrowable Resources”
- Budget Definitions from Dept. of Finance and Legislative Analyst’s Office

California
Home
Enacted
Summary
Revenue
Major Projects
Enacted
K thru 12
Higher Education
Health and Human Services
Corrections
Business and Economic Development
Resources
Environment and Natural Resources
State and Local Government
Labor and Industrial Relations
General
Legislative
Budget

eBudget Search



We want to know what you think!
Please send an e-mail with questions,
comments, and/or concerns regarding
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BUDGET OVERVIEW [Back to Top](#)

[Introduction](#)

The 2008 Budget Act resolves the \$24.3 billion budget deficit identified in the May Revision. It provides a modest reserve of \$1.7 billion this year, but projects a deficit of \$1.0 billion in 2009-10. While this budget does not resolve the state's persistent structural budget deficit, it includes a historic budget reform measure that puts California on the path to fiscal stability and avoids borrowing from local governments or transportation funds.



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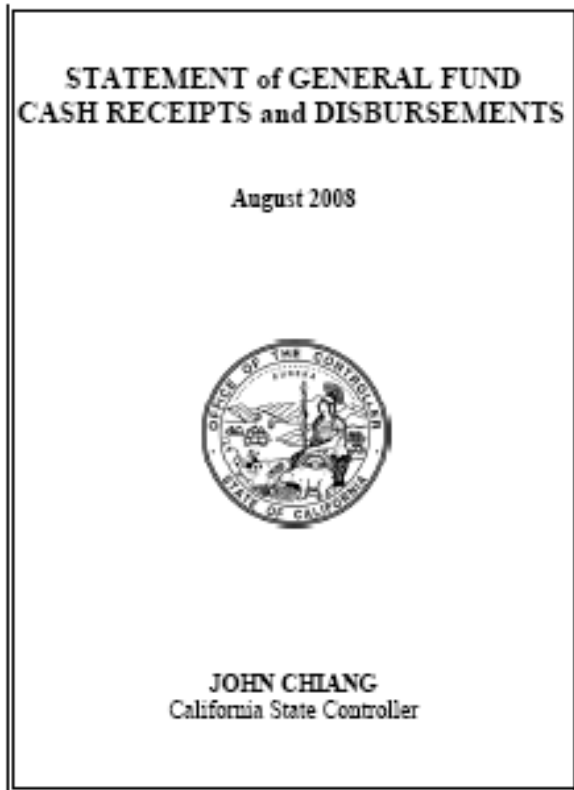
Lots of Other Funds Besides the General Fund:

Examples

- **Film California First Fund**
- **Bicycle Transportation Account**
- **Abandoned Watercraft Abatement Account**
- **Bureau of Thermal Insulation and Home Furnishings Fund**
- **California Collegiate License Plate Fund**



Borrowable Resources



Footnote (g) Additional funds of \$492 million were identified as borrowable and are included in the actual Available Borrowable Resources.

<http://www.sco.ca.gov/ard/cash/0809/aug.pdf>

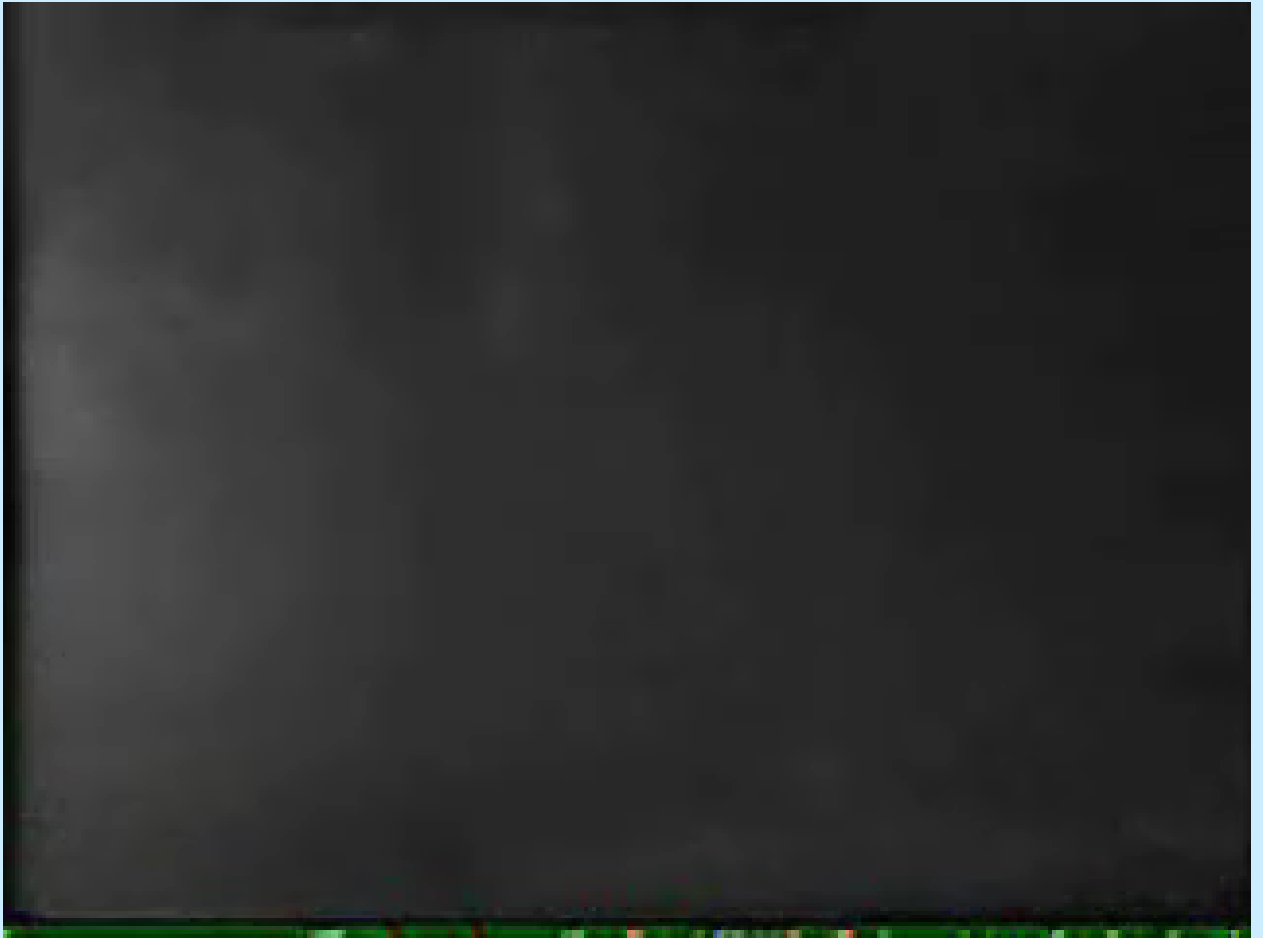




August 2007



What is a “deficit”?



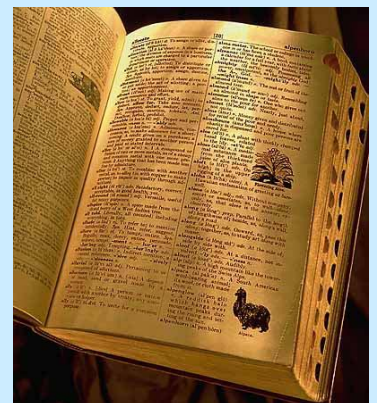
*Does it just mean no money left
to spend?*



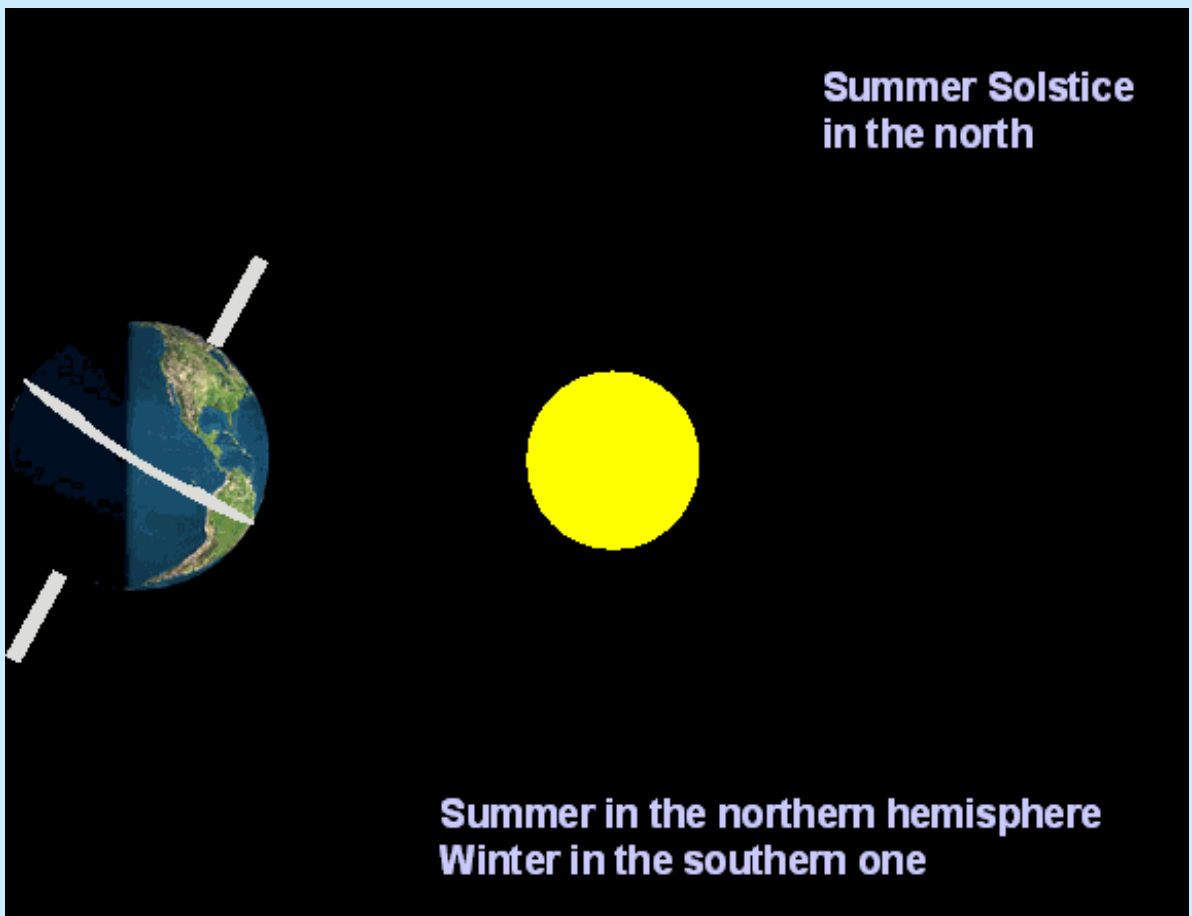
**“Deficit” should mean
income less than
expenditure (a flow concept)**

- *Income = taxes, fees, receipts from feds, interest earned on state funds, etc.*
- *Expenditure = state purchases (including wages), grants to other governments, transfers to individuals, debt service on state debt, etc.*
- *Usually, we refer to the “general fund” when we talk of the state budget deficit or surplus.*

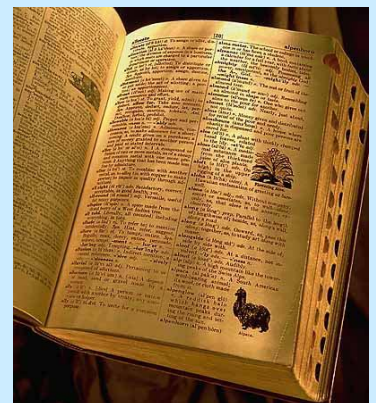
GF = 75-80% of total budget



**“Deficit” should mean
income less than
expenditure...**



...during one year



Sin #1



The term deficit in California-speak is often a confusing multiyear mix of stock and flow

- **Past accumulated deficits in general fund (stock) plus**
- **Estimated current year's deficit (flow) plus**
- **Next year's deficit if we don't do anything (flow)**



\$42 billion!



\$42 billion!



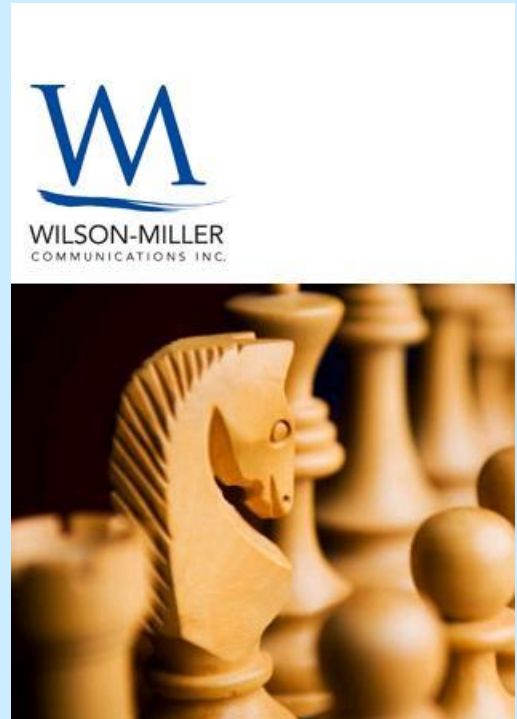


\$42 billion!



Relative to \$100 billion budget?
NO!!

Julie Soderlund, spokesperson for governor and campaign for May 19, 2009 propositions



Budget Reform Now
Yes On Props 1A-1B-1C-1D-1E-1F

**Larry Mantle, Airtalk,
KPCC 3/12/09**

Sin #2



Moreover, borrowing and sales of assets are treated as revenue, often under the heading “revenue and transfers”

Sin #3



Terms such as “shortfall,” “gap,” and “hole” - which have no definition at all - are often used to describe the budget, both by officials and the news media



Short Fall?

Long Fall?





Short Fall?

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Paul Sakuma, Associated Press

California budget faces new \$8-billion shortfall

Plunging revenue has already put the new budget plan out of balance, the state legislative analyst says. The news may complicate the bid to have voters OK special-election measures in May.

By Jordan Rau and Evan Halper
March 14, 2009

Reporting from Sacramento -- The plan that Gov. Arnold Schwarzenegger and





CapitolAlert

THE LATEST ON CALIFORNIA POLITICS AND GOVERNMENT

March 13, 2009

Leaders react to latest budget gap

The legislative leaders who labored for weeks trying to find a way to patch the \$40 billion budget gap closed last month were quick to react today to LAO projections of a new \$8 billion hole.

Senate leader Darrell Steinberg even extended a special invitation to GOP gubernatorial hopefuls Steve Poizner and [Meg Whitman](#), who have been critical of the February budget deal.

Assembly Speaker Karen Bass, D-Los Angeles

"Given the nation's continuing economic problems since we passed the budget, it is not surprising to see the state's revenue projections continue to fall. We must keep a careful watch on revenues during these volatile times, and all of us, Democrats and Republicans alike, must be prepared to continue to make tough decisions should the May Budget Revision also show significant declines in revenue. We also have to keep in our minds the potential that if the [ballot measures](#) fail on May 19th, the budget problem grows by another \$6 billion."

Assembly Republican Leader Mike Villines, R-Clovis



Holes



AP Photo/Timothy



Holes

The Sacramento Bee CapitolAlert



PM Alert: Another \$8 billion hole

In case you missed it today: The Legislature's budget analyst, **Mac Taylor**, declared today that the **immense package of spending cuts, new taxes and loans** aimed at closing the state's \$40 billion budget deficit will **fall short by \$8 billion** because the state's economy is continuing to falter.

The **legislative leaders who labored for weeks** trying to find a way to patch the \$40 billion budget gap were quick to react today to LAO projections of a new \$8 billion hole.

When it comes to **protecting children's interests, nobody scores 100 percent** in the California Legislature, according to the San Diego-based Children's Advocacy Institute.



AP Photo/David Hume



Shortfall, gap, hole?

THE SACRAMENTO BEE sacbee.com **Capitol Alert**

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Friday, March 13, 2009 **SEARCH**

 **CapitolAlert**

THE LATEST ON CALIFORNIA POLITICS AND GOVERNMENT

March 13, 2009

Budget analyst sees new \$8 billion deficit

The Legislature's budget analyst, Mac Taylor, declared today that the immense package of spending cuts, new taxes and loans aimed at closing the state's \$46 billion budget deficit will fall short by \$8 billion because the state's economy is continuing to falter.

Deficit?

Leg Analyst Uses “Surplus” and “Deficit” as a Stock in Media Conference of 3/13/09

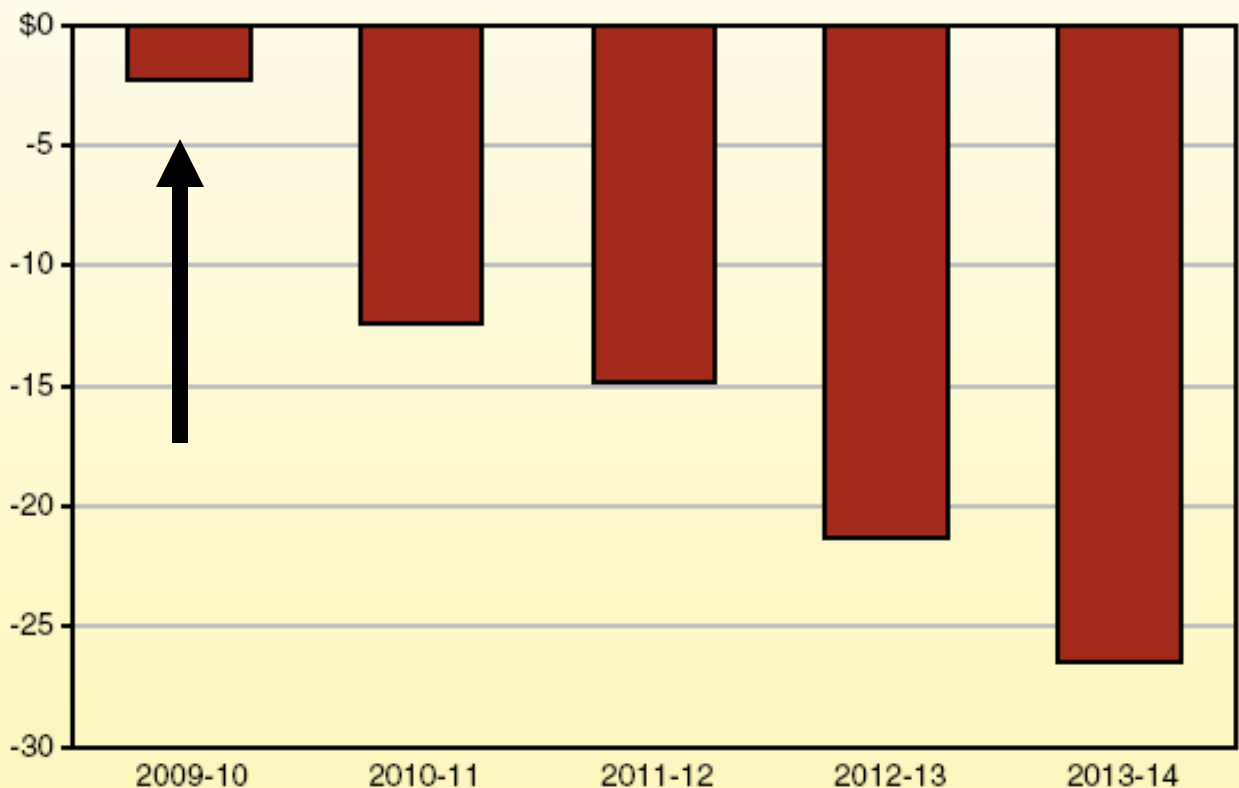


**He is talking about the projected
reserve (stock concept) in the GF
as of 6/30/10**

His chart for that media conference shows a (flow) deficit of -\$2.5 billion for FY 2009-10...

Operating Shortfalls Projected to Grow Dramatically Throughout Forecast Period

General Fund (In Billions)



...but calls it a “shortfall.”

CALIFORNIA STATEWIDE SPECIAL ELECTION

Tuesday, May 19, 2009 ★ Official Voter Information Guide

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[Secretary of State](#)

[Elections](#)

[Political Reform](#)

Voter Information Guide (VIG)

[Proposition 1A](#)

[Proposition 1B](#)

[Proposition 1C](#)

[Proposition 1D](#)

[Proposition 1E](#)

[Proposition 1F](#)

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Quick Reference Guide

[Proposition 1A](#)

[Proposition 1B](#)

[Proposition 1C](#)

[Proposition 1D](#)

[Proposition 1E](#)

[Proposition 1F](#)

<http://www.voterguide.sos.ca.gov/quick-reference-guide/index.htm>

OH, GAWD!
NOT ANOTHER
ELECTION!



May 19 Special Election

- **1A: State Budget. Changes California Budget Process. Limits State Spending. Increases "Rainy Day" Budget Stabilization Fund.**
 - *PS: Extends tax increases 1-2 years, limited midyear cut authority*

Jan Tinbergen
Nobel 1969

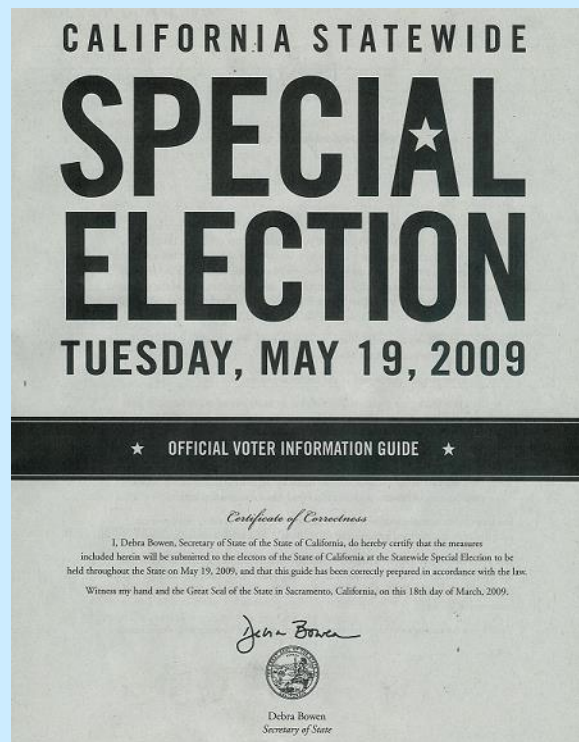


May 19 Special Election

- **1A: State Budget. Changes California Budget Process. Limits State Spending. Increases "Rainy Day" Budget Stabilization Fund.**

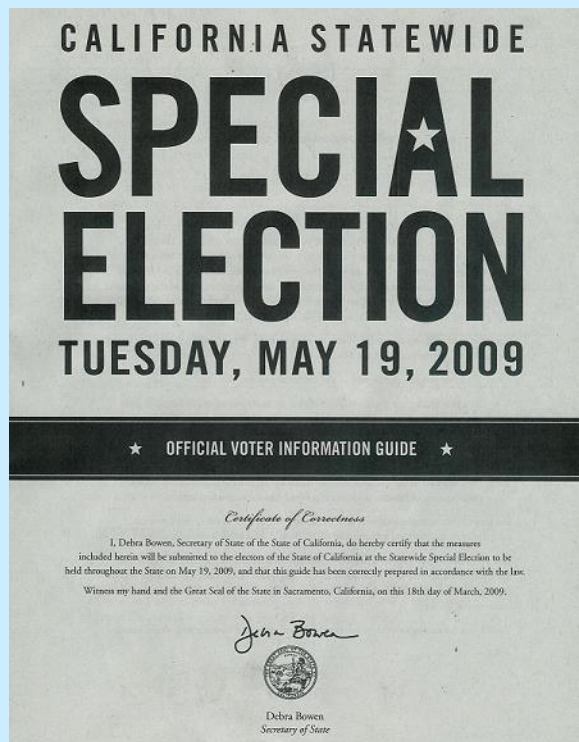
– *PS: Extends tax increases 1-2 years, limited midyear cut authority*

**pp. 47-48: Adds
Section 21 to
Article XVI of
California
constitution**



May 19 Special Election

*Sec. 21(d)(1):
The General
Fund revenues
for the current
fiscal year shall
be forecast by
extrapolating
from the trend
line derived by a
linear regression
of General Fund
revenues as a
function of fiscal
year for the
period of the 10
fiscal years.*



May 19 Special Election

- **1A: State Budget. Changes California Budget Process. Limits State Spending. Increases "Rainy Day" Budget Stabilization Fund.**
 - *PS: Extends tax increases 1-2 years, limited midyear cut authority*
- **1B: Education Funding. Payment Plan.**
 - *K-14 Prop 98 pay back 2011-12 and beyond*
- **1C: Lottery Modernization Act.**
 - *aka borrowing against lottery*



May 19 Special Election

- **1D: Protects Children's Services Funding. Helps Balance State Budget.**
 - *Redirects (i.e., takes) First-5 early childhood tobacco funds from Prop 10 of 1998*

May 19 Special Election

- **1D: Protects Children's Services Funding. Helps Balance State Budget.**
 - *Redirects (i.e., takes) First-5 early childhood tobacco funds from Prop 10 of 1998*



May 19 Special Election

- **1D: Protects Children's Services Funding. Helps Balance State Budget.**
 - *Redirects (i.e., takes) First-5 early childhood tobacco funds from Prop 10 of 1998*
- **1E: Mental Health Services Funding. Temporary Reallocation. Helps Balance State Budget.**
 - *Redirects mental health funds from tax on millionaires of Prop 63 (2004)*
- **1F: Elected Officials' Salaries. Prevents Pay Increases During Budget Deficit Years.**

Prop 1A: Cap, Rainy Day, Limited Cut Authority, Tax Extension



Groping for a Solution



Long-term solution proposed by governor along with his January 2008 budget message:

Rainy Day Fund



Caveat Voter



You can only accumulate a rainy day fund when the Sun is shining. What we could have done in the past doesn't fix today's problem.

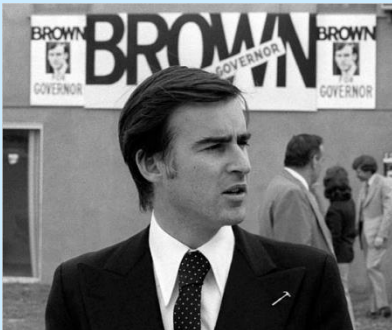
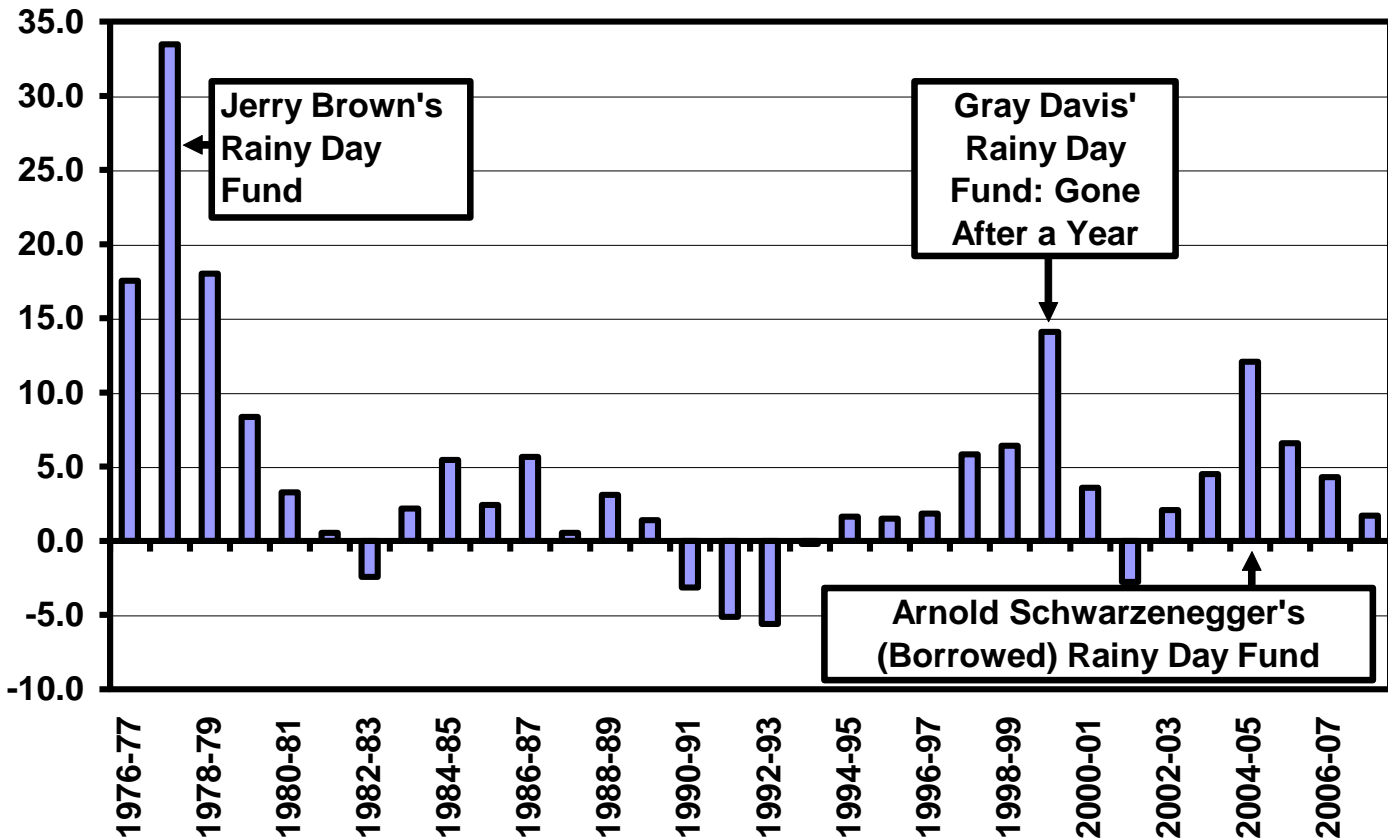
Caveat Voter



The rainy day fund the governor would like to mandate (about 1/8th of the GF) is roughly what Gray Davis had at the dot-com peak.



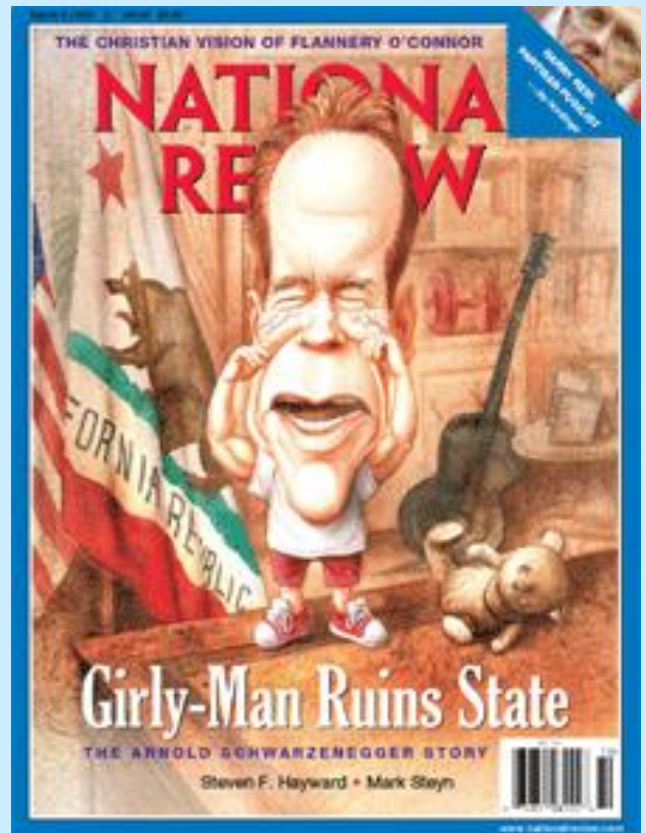
End of Year GF Reserve as % of Expenditures



John and Ken: KFI Radio

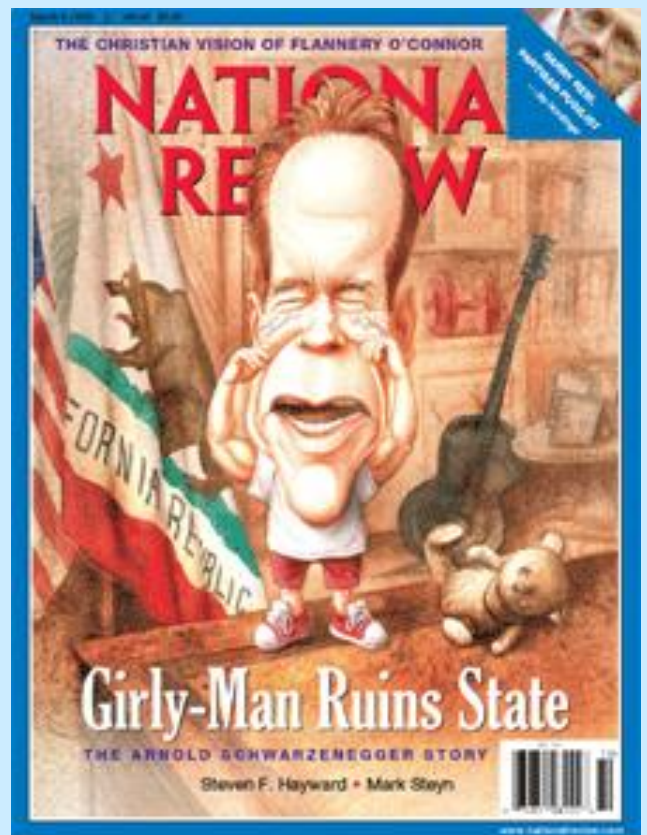


**Revolt
on the
Right**





Revolt on the Right





Prop 1B contingent on Prop 1A

CALIFORNIA
TEACHERS
ASSOCIATION



Prop 1B contingent on Prop 1A

CALIFORNIA
TEACHERS
ASSOCIATION





Prop 1B contingent on Prop 1A

CALIFORNIA
TEACHERS
ASSOCIATION



Prop 1B contingent on Prop 1A

CALIFORNIA
TEACHERS
ASSOCIATION





1A and 1B Have No Immediate Effect on State Budget



...with a possible exception

1A and 1B Have No Immediate Effect on State Budget



...with a possible exception

Prop 1C - Lottery


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Lottery


GTECH, the world leader in gaming technology, supplies end-to-end lottery services and lottery game content. We offer world-class system design, delivery, and ongoing support operations; terminal installation and maintenance; retailer training; marketing support; field service; hotline management; telecommunications network installation, management and maintenance; and a diverse portfolio of games for each channel of distribution.





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PRINTED PRODUCTS

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- DIVERSIFIED GAMING
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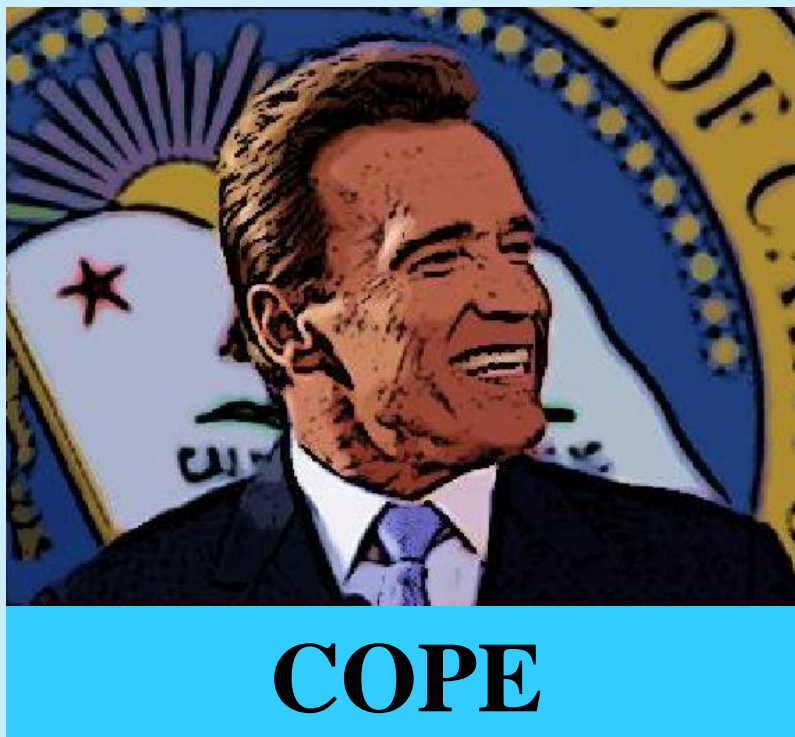
PRINTED PRODUCTS

As growth of the instant lottery ticket category continues to change the manufacturing, finishing and game programming paradigm, Scientific Games has been challenged to step forward and invest in this new environment.

We have answered the challenge with a sweeping, multi-year, \$45 million investment in new processes, new systems and new technology to enhance and extend our worldwide manufacturing operations, particularly in the U.S. and England. These forward-thinking investments mean we now have the 3 *newest presses* in the industry.

In the \$50 billion-plus U.S. lottery market, instant ticket category growth continues to outpace online lottery products. Our investment strategically aligns with this growth and coincides with a trend among lotteries internationally to lean more heavily on the instant category for incremental revenue.







COPE



HOPE

Pre-Election





COPE



Post-Election





COPE



Post-Election





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Post-Election





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HOPE

Stimulus Funds for California?





COPE



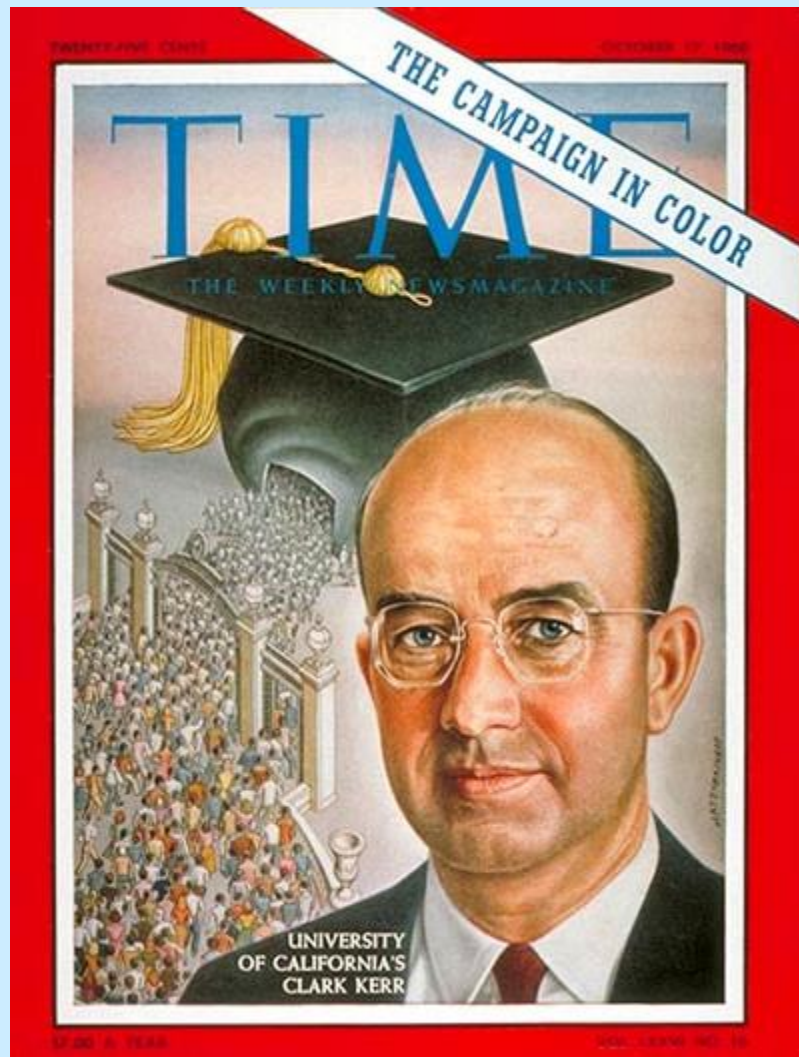
HOPE

Stimulus Funds for California?





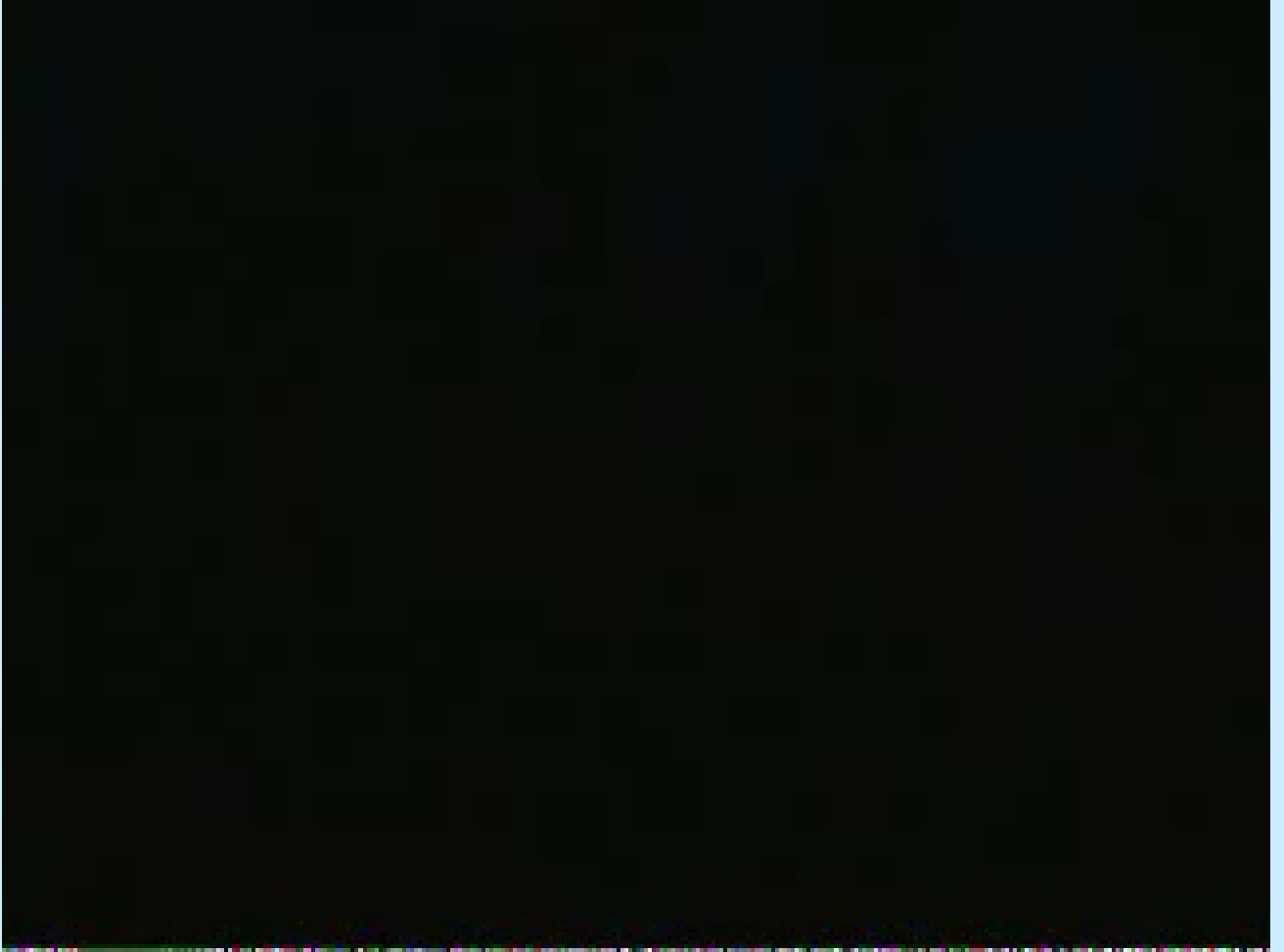
Implications for UC and Higher Ed



Time: Oct. 17, 1960

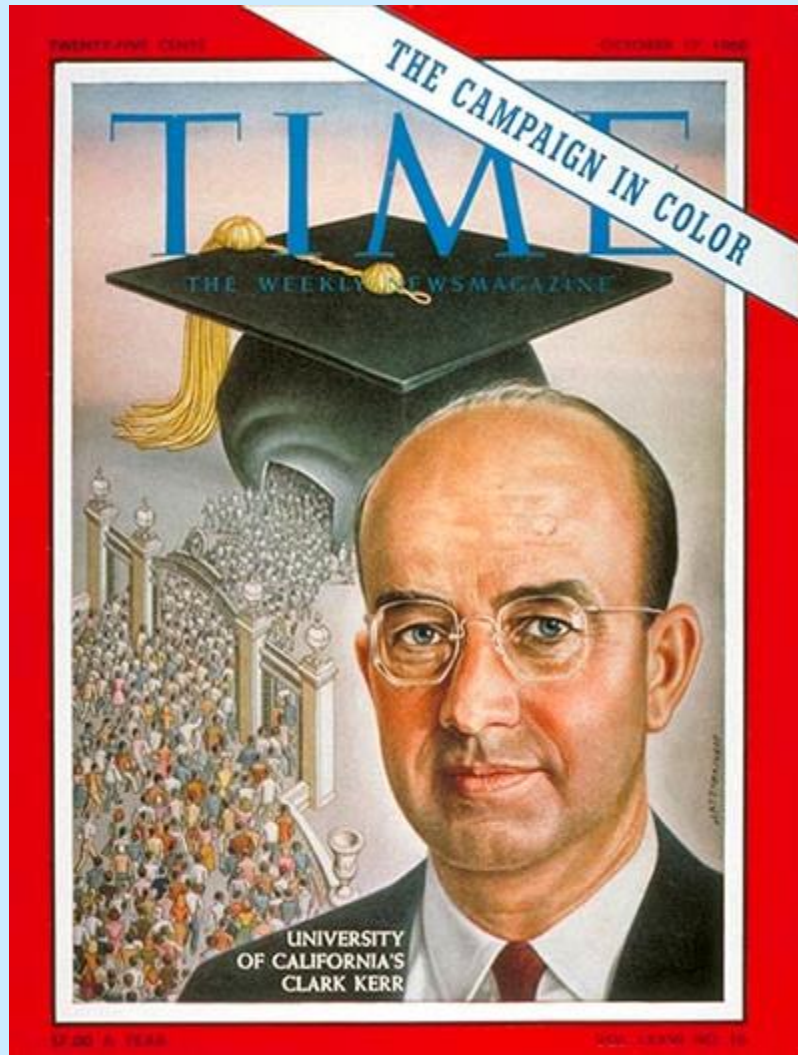


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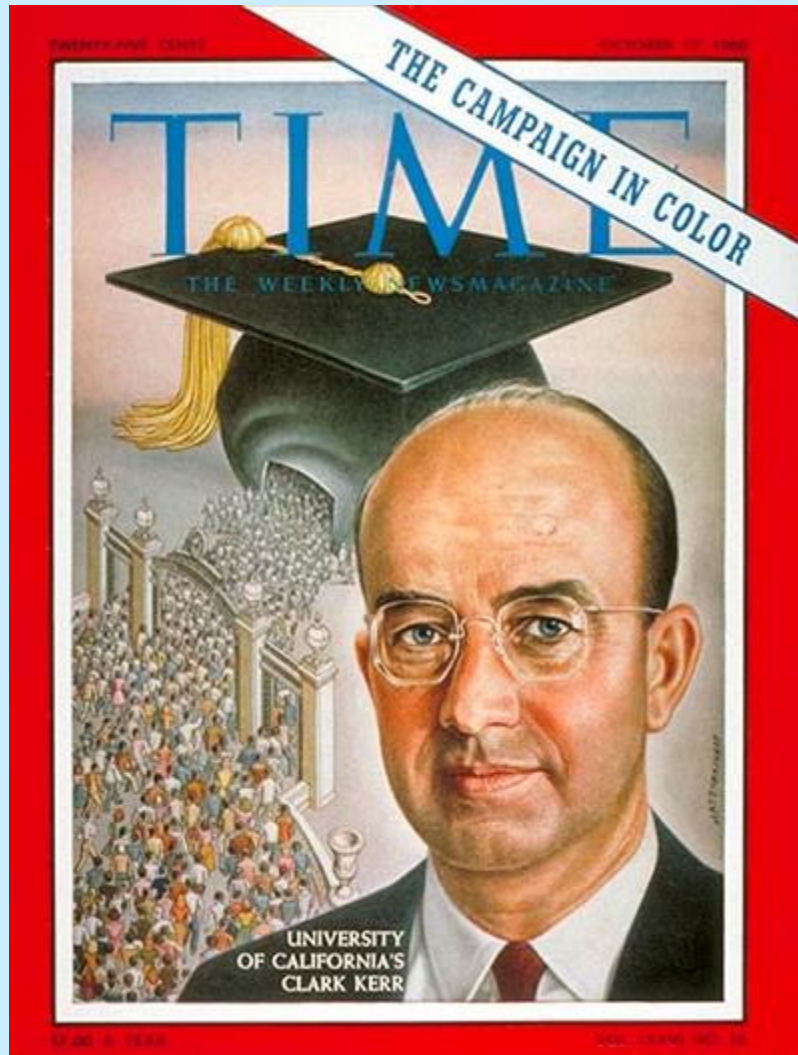
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California's Budget Crisis



Daniel J.B. Mitchell

May 7, 2009

UCLA-SPA